

Legislative
Assembly of
Ontario



Assemblée
législative de
l'Ontario

STANDING COMMITTEE ON PUBLIC ACCOUNTS

PUBLIC ACCOUNTS OF THE PROVINCE

(Chapter 2, 2014 Annual Report of the Auditor General of Ontario)

1st Session, 41st Parliament
65 Elizabeth II

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The Honourable Dave Levac, MPP
Speaker of the Legislative Assembly

Sir,

Your Standing Committee on Public Accounts has the honour to present its Report and commends it to the House.

Ernie Hardeman, MPP
Chair of the Committee

Queen's Park
April 2016

STANDING COMMITTEE ON PUBLIC ACCOUNTS

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1st Session, 41st Parliament

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PREAMBLE

On November 4, 2015 the Standing Committee on Public Accounts held a public hearing on an audit of the Public Accounts of the Province (Chapter 2, *2014 Annual Report* of the Auditor General of Ontario).

The Committee endorses the Auditor's findings and recommendations, and presents its findings, views, and recommendations in this report. The Committee requests that the Treasury Board Secretariat, the Ministry of Finance, and the Ontario Financing Authority officials provide the Clerk of the Committee with written responses to the recommendations within 120 calendar days of the tabling of the report with the Speaker of the Legislative Assembly, unless otherwise specified.

ACKNOWLEDGEMENTS

The Committee extends its appreciation to officials from the Treasury Board Secretariat, the Ministry of Finance, and the Ontario Financing Authority who appeared before the Committee on November 4, 2015. The Committee also acknowledges the assistance provided during the hearings and report writing deliberations by the Office of the Auditor General, the Clerk of the Committee, and staff in the Legislative Research Service.

OVERVIEW

The government is responsible for preparing the consolidated financial statements and ensuring that this information, including many amounts based on estimates and judgment, is presented fairly. The government is also responsible for ensuring that an effective system of control, with supporting procedures, is in place to authorize transactions, safeguard assets, and maintain proper records.

AUDIT OBJECTIVES AND SCOPE

The Auditor's office audits the consolidated financial statements, with the objective of providing reasonable assurance that the statements are free of significant errors or omissions. The consolidated financial statements, along with the independent Auditor's Report, are included in the Province's annual report.

The chapter resulting from the audit of the Public Accounts of the Province (Chapter 2, *2014 Annual Report* of the Auditor General of Ontario) focused on Ontario's growing debt burden, and the critical implications this has for the Province's finances. The Auditor indicated that "increases in the debt are attributable to continued government borrowing to finance deficits and infrastructure spending."¹

¹ Office of the Auditor General of Ontario, *2014 Annual Report*, Chapter 2: Public Accounts of the Province, p. 31.

ISSUES RAISED IN THE AUDIT AND BEFORE THE COMMITTEE

While a number of issues were raised in the audit and before the Committee, those discussed below are considered to be particularly important.

INCREASING DEBT BURDEN

AUDITOR'S RECOMMENDATION

In order to address the province's growing total debt burden, the government should work toward the development of a long-term total debt reduction plan.

The government has relied on historically low interest rates to keep its debt-servicing costs relatively stable, but the debt itself continues to grow (at a declining rate) regardless of which measure—total debt, net debt, or accumulated deficit—is used to assess it.

Total Debt, Net Debt and Accumulated Deficit, 2009/10 – 2017/18 (\$ millions)

	Actual					Estimate			
	2009/10 ¹	2010/11 ¹	2011/12 ¹	2012/13 ¹	2013/14 ²	2014/15 ¹	2015/16 ¹	2016/17 ¹	2017/18 ³
Total debt	212,122	236,629	257,278	281,065	295,758	310,549	326,600	337,800	345,600
Net debt	193,589	214,511	235,582	252,088	267,190	289,251	305,300	317,200	325,000
Accumulated deficit	130,957	144,573	158,410	167,132	176,634	189,765	198,600	204,000	204,000

1. 2014 Ontario Budget

2. March 31, 2014 Province of Ontario Consolidated Financial Statements

3. Office of the Auditor General of Ontario

Source: Office of the Auditor General of Ontario, *2014 Annual Report*, p. 35.

During the hearing, government officials noted as follows:

- Mr. Thompson testified that the government is committed to eliminating the annual deficit by 2017-18, and that Ontario has reported lower-than-projected program expense and a lower-than-forecast deficit six years in a row.
- Mr. Thompson testified that over the past four years, the average annual growth in program spending has been held to 1.4%, less than the rate of inflation.
- Mr. Mayman testified that the government has committed to reducing Ontario's net debt-to-GDP ratio to its pre-recession level of 27%, and that the government's borrowing plan has consistently kept interest on debt costs below budget projections.

- Mr. Mayman said that the net debt-to-GDP ratio is a key financial indicator because it represents the affordability of debt.
- Mr. Mayman also noted that by utilizing term extensions, the government locks in low interest rates for longer periods, which reduces refinancing risks and helps offset the impact of higher interest rates.
- Mr. Mayman testified that while credit ratings are an important component of the province's creditworthiness, there are other equally (or more) important measures, such as investor receptivity of the government's debt.
 - Mr. Mayman noted that domestic and international investors continue to be avid buyers of Ontario debt through the purchase of government bonds.

Committee Recommendation

The Standing Committee on Public Accounts recommends that:

- 1. Officials provide details on the government's long-term debt reduction plan of reducing net debt-to-GDP ratio from 2013/14 levels of 38.6% to pre-recession levels of 27%.²**

(A response is requested within 60 days of the tabling of the report with the Speaker of the Legislative Assembly.)

- 2. Officials provide clarification and further details on measures to be taken relating to the statement that "the government is committed to eliminating the annual deficit by 2017-18."**

(A response is requested within 60 days of the tabling of the report with the Speaker of the Legislative Assembly.)

- 3. Officials provide supporting data confirming that average annual growth in program spending has been held to 1.4% less than the rate of inflation.**

(A response is requested within 60 days of the tabling of the report with the Speaker of the Legislative Assembly.)

² The *Ontario Finances 2015-16 First Quarter Update* notes that Ontario's net debt-to-GDP ratio is expected to peak at 39.8% in 2015-16, consistent with the forecast in the 2015 Ontario Budget.

ELECTRICITY SECTOR STRANDED DEBT

Stranded debt arose under the *Energy Competition Act, 1998*, with the major restructuring of the electricity industry. The Ontario Electricity Financial Corporation (OEFC) was given the responsibility to manage the legacy debt of the old Ontario Hydro and certain other liabilities not transferred to Hydro One or Ontario Power Generation (OPG).

The OEFC inherited \$38.1 billion in total debt and other liabilities from Ontario Hydro when the electricity market was restructured on April 1, 1999. Only a portion of the \$38.1 billion was supported by the value of the assets of Hydro One, OPG, and the Independent Electricity System Operator, leaving \$20.9 billion of stranded debt not supported by assets.

The government's long-term plan to service and retire the \$20.9 billion in stranded debt included dedicating revenue streams to OEFC to help pay down this debt. Future revenue streams from electricity-sector companies would eliminate \$13.1 billion of the debt. The remaining \$7.8 billion (the residual stranded debt) would be recovered through a debt retirement charge.

During the hearing, government officials noted the following:

- Mr. Kwan testified that effective May 2012, the Ministry of Finance is required by regulation (O.Reg 89/12: Residual Stranded Debt) to provide an annual determination of the remaining residual stranded debt.³
- Mr. Kwan testified that the next determination of residual stranded debt will be current to March 31, 2015 and has to be provided publicly by March 31, 2016.⁴
- Mr. Kwan testified that there are many variables involved in the calculation of residual stranded debt—it is a fairly complex formula that determines the amount annually.
 - The amount of residual stranded debt can go up or down, as future projections are subject to considerable uncertainty.
 - Payments to the residual stranded debt go not just to the base amount remaining, but to interest on that amount.
 - Other factors, such as a freeze on energy prices, can cause the residual stranded debt to increase.

³ O. Reg 89/12 was revoked on February 11, 2016.

⁴ The revocation of O. Reg 89/12 removes the requirement to provide a public update on the determination of residual stranded debt.

Committee Recommendation

The Standing Committee on Public Accounts recommends that:

4. **Officials provide an update on specific impacts of removing the debt retirement charge from residential users' electricity bills after December 31, 2015.**
5. **Officials provide an update on what impact the *Budget Measures Act, 2015* may have on the residual stranded debt as it relates to calculating and repaying this debt.**

ECONOMY AND GOVERNMENT SPENDING

General discussions during the hearings related to the state of the economy moving forward and the impact this may have on Ontario's Public Accounts. Committee members also asked why certain program areas had lower-than-forecast spending.

During the hearing, government officials noted the following:

- Mr. Thompson testified that officials have regular conversations with the Minister of Finance regarding economic conditions and the impact they may have on government finances.
- Mr. Thompson testified that at least twice annually, private sector economists are polled regarding current economic conditions.
- Mr. Orencsak testified that in 2013-14, approximately two-thirds of ministries spent below their original budget allocations.
 - For example, lower spending by school boards was a result of lower-than-forecast student enrollment growth.
- Mr. Orencsak testified that program review, renewal, and transformation is a new approach the government launched last year to support multi-year planning and budgeting. It is a government-wide process that asks the following questions when looking at a program:
 - Is the program achieving desired outcomes in the most effective way possible?
 - Is program delivery happening as efficiently as possible?
 - Is a program sustainable?

CONSOLIDATED LIST OF COMMITTEE RECOMMENDATIONS

The Standing Committee on Public Accounts recommends that:

1. **Officials provide details on the government's long-term debt reduction plan of reducing net debt-to-GDP ratio from 2013/14 levels of 38.6% to pre-recession levels of 27%.⁵**

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⁵ The *Ontario Finances 2015-16 First Quarter Update* notes that Ontario's net debt-to-GDP ratio is expected to peak at 39.8% in 2015–16, consistent with the forecast in the 2015 Ontario Budget.